No. 82-1805

In the Supreme Court of the United States

OCTOBER TERM, 1982

JOHNSON COUNTY MEMORIAL HOSPITAL, ET AL., PETITIONERS

v.

MARGARET M. HECKLER, SECRETARY OF HEALTH AND HUMAN SERVICES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether hospitals that provide free care to indigents as a condition to receiving federal construction subsidies under the Hill-Burton Act, 42 U.S.C. 291 *et seq.*, are entitled to receive federal Medicare reimbursement for a portion of that free care.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A14-A20) is reported at 698 F.2d 1347. The opinion of the district court (Pet. App. A1-A13) is reported at 527 F. Supp. 1134.

JURISDICTION

The judgment of the court of appeals was entered on February 1, 1983. The petition for a writ of certiorari was filed on May 2, 1983. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES INVOLVED

42 U.S.C. 1395x(v)(1)(A) provides in pertinent part:

> The reasonable cost of any services shall be * * * the cost actually incurred, excluding therefrom any part of

incurred cost found to be unnecessary in the efficient delivery of needed health services, and shall be determined in accordance with regulations establishing the method or methods to be used, and the items to be included, in determining such costs * * *. Such regulations shall (i) take into account both direct and indirect costs of providers of services (excluding therefrom any such costs, including standby costs, which are determined in accordance with regulations to be unnecessary in the efficient delivery of services covered by the insurance programs established under this subchapter) in order that, under the methods of determining costs, the necessary costs of efficiently delivering covered services to individuals covered by the insurance programs established by this subchapter will not be borne by individuals not so covered, and the costs with respect to individuals not so covered will not be borne by such insurance programs, and (ii) provide for the making of suitable retroactive corrective adjustments where, for a provider of services for any fiscal period, the aggregate reimbursement produced by the methods of determining costs proves to be either inadequate or excessive.

42 U.S.C. (& Supp. V) 1395y provides in pertinent part:

(a) Items or services specifically excluded

Notwithstanding any other provision of this subchapter, no payment may be made under part A or part B for any expenses incurred for items or services —

* * * * *

(2) for which the individual furnished such items or services has no legal obligation to pay, and which no other person (by reason of such individual's membership in a prepayment plan or otherwise) has a legal obligation to provide or pay for;

(3) which are paid for directly or indirectly by a governmental entity (other than under this chapter and other than under a health benefits or insurance plan established for employees of such an entity), except in * * * such * * * cases as the Secretary may specify; * * *

STATEMENT

Petitioners are 51 hospitals that applied for and received federal construction subsidies under the Hill-Burton Act, 42 U.S.C. 291 *et seq.* As a statutory condition to receipt of the Hill-Burton subsidies, see 42 U.S.C. 291c(e), petitioners promised to provide a reasonable volume of free medical care to indigent persons. The Hill-Burton regulations exclude from the computation of free medical care "[a]ny amount which the [hospital] has received, or is entitled to receive, * * * under a governmental program." 42 C.F.R. 53.111(f)(2)(i).

Petitioners also are providers of medical services under the federal Medicare program (42 U.S.C. (& Supp. V) 1395 *et seq.*). That program reimburses providers for their "reasonable costs" incurred in treating Medicare patients. The "reasonable cost" of any service is "the cost actually incurred," and is to be "determined in accordance with regulations" promulgated by the Secretary of Health and Human Services. 42 U.S.C. 1395x(v)(1)(A). These regulations must "take into account * * * [providers'] direct and indirect costs," but may not impose Medicare costs on non-Medicare patients, or conversely, impose non-Medicare costs on the Medicare program. *Ibid.* In addition, the Medicare program provides no reimbursement if the individual receiving medical care "has no legal obligation to pay" for the care or if a government entity pays "directly or indirectly" for the individual's care. 42 U.S.C. 1395y(a)(2) and (a)(3). The Secretary's Medicare regulations expressly

exclude "charity allowances" — defined as "reductions in charges made by the provider of services because of the indigence or medical indigence of the patient" — from reimbursement. 42 C.F.R. 405.420(a) and (b)(2).

Each of the petitioners attempted to obtain Medicare reimbursement for a portion of its expenditures for the free care it was required to provide as a condition to receiving Hill-Burton funds. The Provider Reimbursement Review Board denied the claims, and petitioners filed suit challenging that decision in the United States District Court for the Southern District of Indiana. The district court rejected as "arbitrary and capricious" the Secretary's position that Medicare reimbursement is not available to cover free care costs, since the court believed that such costs are "indirect costs" within the meaning of the Medicare legislation (Pet. App. A1-A13). The Secretary appealed.

While the case was on appeal, Congress passed the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), Pub. L. No. 97-248, 96 Stat. 324. Section 106 of TEFRA (96 Stat. 337) amended the Medicare statute to state (1) that the Secretary's Medicare regulations "shall provide" that a hospital's costs in providing Hill-Burton free care to indigents are not reimbursable as "reasonable costs";[1] and (2) that the amendment "shall be effective" with respect to "any" Hill-Burton costs, except for those previously allowed by a final court of appeals judgment. The Conference Report that accompanied TEFRA expressly states that the purpose of Section 106 was merely to "clarify that Hill-Burton free care costs have never been, and are not, allowable for medicare reimbursement purposes." H.R. Rep. No. 97-760, 97th Cong., 2d Sess. 431 (1982).

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[1]The Secretary promulgated the regulations mandated by Section 106 on October 1, 1982. See 47 Fed. Reg. 43656-43658, to be codified at 42 C.F.R. 405.420.

The court of appeals reversed (Pet. App. A14-A20). Citing its decision in *Saint Mary of Nazareth Hospital Center* v. *HHS*, 698 F.2d 1337 (7th Cir. 1983), decided the same day, the court held that the retroactive application of Section 106 is constitutional and that the Secretary acted properly in adhering to his longstanding policy of disallowing Medicare reimbursement for the costs hospitals incur in providing a reasonable number of indigent persons with free care in partial fulfillment of Hill-Burton obligations. The court of appeals rejected petitioners' position that they had a vested contractual right to Medicare reimbursement of the costs at issue. The court concluded that the two statutes are separate federal aid programs and that Congress had never intended to provide Medicare reimbursement for the free care hospitals must provide under the terms of the Hill-Burton Act. The court stated, "it would be improper to allow the hospitals to receive a double payment from the government, and Congress did not intend to compensate hospitals a second time for medical care for which the government has already paid through contractual agreements for indigent care under the Hill-Burton Act" (Pet. App. A20).

ARGUMENT

The court of appeals' decision is correct and is in accord with the decisions of five other courts of appeals.[2] Moreover,

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[2] *Memorial Hospital* v. *Heckler*, No. 81-6230 (11th Cir. June 6, 1983); *Catholic Medical Center* v. *New Hampshire-Vermont Hospitalization Service, Inc.*, No. 82-1808 (1st Cir. May 4, 1983); *Iredell Memorial Hospital, Inc.* v. *Schweiker*, 699 F.2d 196 (4th Cir. 1983); *Metropolitan Medical Center* v. *Harris*, 693 F.2d 775 (8th Cir. 1982); *Harper-Grace Hospitals* v. *Schweiker*, 691 F.2d 808 (6th Cir. 1982). See also *Saint Mary of Nazareth Hospital Center* v. *HHS*, 698 F.2d 1337 (7th Cir. 1983). But see *Presbyterian Hospital* v. *Harris*, 638 F.2d 1381 (5th Cir.), cert. denied on a different issue, 454 U.S. 940 (1981), decided prior to passage of Section 106 of TEFRA.

because Congress has recently amended the Medicare statute to make clear that free care provided under the Hill-Burton Act is not a reimbursable expense, the issue is of no continuing importance. Thus, further review is not warranted.

1. The Secretary's longstanding interpretation of the Medicare statute as precluding reimbursement for Hill-Burton free care costs is grounded in a number of statutory and regulatory provisions. That interpretation is reasonable and should be accorded deference. See *Zenith Radio Corp.* v. *United States,* 437 U.S. 443, 450-451 (1978); *Batterton* v. *Francis,* 432 U.S. 416, 425 (1977).

The language of the Medicare statute and the regulations promulgated under the statute support the Secretary's interpretation in several respects. First, while the reasonable cost provision of the Medicare statute states that "indirect costs" are reimbursable, the same section explicitly provides that the Secretary is to determine the precise availability of Medicare reimbursement through promulgation of regulations. 42 U.S.C. 1395x(v)(1)(A). The Secretary has exercised that express regulatory authority to exclude from reimbursement "charity" expenses, which include costs of free care to indigent individuals, as well as certain other "indirect" expenses, such as bad debts, courtesy allowances, and some research costs. See 42 C.F.R. 405.420(a), 405.422. This exclusion plainly is not unreasonable.[3] Both the common understanding of the term "charity" and judicial authority support the Secretary's conclusion that free care provided as a condition of receiving Hill-Burton funds constitutes "charity" and is therefore not reimbursable under

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[3]The Secretary has explained that bad debts, charity, and courtesy allowances are reductions in revenue, and do not add to the cost of providing services, since such costs "have already been incurred in the production of the services." 42 C.F.R. 405.420(c).

the Medicare program. See, *e.g., American Hospital Ass'n* v. *Harris,* 625 F.2d 1328, 1330 (7th Cir. 1980); *Cook* v. *Ochsner Foundation Hospital,* 559 F.2d 968, 972, 973 (5th Cir. 1977).

Second, at least three provisions of the Medicare statute itself suggest that Hill-Burton free care costs are not reimbursable: (1) 42 U.S.C. 1395x(v)(1)(A), which precludes Medicare reimbursement for the cost of care of non-Medicare patients; (2) 42 U.S.C. 1395y(a)(2), which excludes Medicare coverage in cases in which the patient has no legal "obligation to pay"; and (3) 42 U.S.C. 1395y(a)(3), which excludes Medicare reimbursement in cases in which the care already has been "paid for * * * indirectly" by another government program. Hill-Burton patients are non-Medicare patients, they incur no obligation to pay, and their care has already been "paid for" by funding from another government program, *i.e.,* Hill-Burton subsidies.

In addition, the language of the Hill-Burton Act supports the Secretary's interpretation. The Act expressly imposes on hospitals a duty to provide free care; it also establishes an exception to this duty if it is not feasible from a financial viewpoint. 42 U.S.C. 291c(e). The financial infeasibility provision indicates that Congress anticipated that hospitals would devote their own resources to meeting the free care obligation. See *Catholic Medical Center* v. *New Hampshire-Vermont Hospitalization Service, Inc.,* No. 82-1808 (1st Cir. May 4, 1983), slip op. 8-9. See also the Secretary's Hill-Burton regulations, which exclude from the computation of free medical care any amount a hospital has received under a governmental program. 42 C.F.R. 53.111(f)(2).

Medicare reimbursement for Hill-Burton free care would undercut the policy of the Hill-Burton Act to require hospitals themselves to provide free care as a condition of federal construction aid. The promise petitioners made in return

for receipt of Hill-Burton subsidies would be virtually meaningless if all it requires is that petitioners apply to the government for reimbursement of expenses incurred in fulfilling the promise. That interpretation of the Medicare statute in effect would require the federal government to pay twice for petitioners' commitment to provide free care for indigents. As the court below noted in a companion case, petitioners' interpretation "would put the government in the anomalous position of acting as a permanent life support system for health care facilities who provide services for the indigent without requiring that the hospitals fulfill the contractual obligations they incurred when accepting Hill-Burton funds." *Saint Mary of Nazareth Hospital Center* v. *HHS*, 698 F.2d 1337, 1344 (7th Cir. 1983). There is no support in the legislative history of either statute for such a result. See, *e.g.*, *id.* at 1343; *Metropolitan Medical Center* v. *Harris*, 693 F.2d 775, 783-785 (8th Cir. 1982). See also *Catholic Medical Center* v. *New Hampshire-Vermont Hospitalization Service, Inc., supra; Iredell Memorial Hospital, Inc.* v. *Schweiker*, 699 F.2d 196 (4th Cir. 1983). As the legislative history of Section 106 of TEFRA confirms, "Hill-Burton free care costs have never been * * * allowable for medicare reimbursement purposes." H.R. Rep. No. 97-760, 97th Cong., 2d Sess. 431 (1982).[4]

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[4]Petitioners cite *Presbyterian Hospital* v. *Harris, supra*, as in conflict with the circuits that have rejected petitioners' interpretation. The Fifth Circuit concluded in *Presbyterian Hospital* that Hill-Burton free care costs would qualify for Medicare reimbursement because they are "indirect costs" and because they are similar to reimbursable interest costs. However, the Secretary, who is given express statutory authority to define the availability of Medicare reimbursement, has defined indirect costs to include interest and depreciation expenses, but not Hill-Burton free care costs. See 42 C.F.R. 405.415-405.419. The Secretary's treatment of free care costs as reductions in revenue, rather than as asset depletion expenses, is not unreasonable. See *Catholic Medical Center*

2. Petitioners further contend (Pet. 10-14) that Congress may not constitutionally bar their claims for reimbursement of Hill-Burton free care costs through retroactive application of Section 106 of TEFRA.[5] They assert that Section 106 abrogates their vested contract rights to reimbursement and constitutes an unconstitutional "taking" of property. These contentions are unpersuasive.

As the preceding section makes clear, petitioners are mistaken in assuming that Section 106 constitutes new law. Congress enacted Section 106 simply to "clarify that Hill-Burton free care costs have never been, and are not, allowable for medicare reimbursement purposes." H.R. Rep. No.

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v. *New Hampshire-Vermont Hospitalization Service, Inc., supra,* slip op. 8.

To the extent there is a conflict between *Presbyterian Hospital* and the cases from other circuits, that conflict is of little significance. After *Presbyterian Hospital* was decided, Congress enacted Section 106 of TEFRA, which will govern any future cases in this area. See pages 9-13, *infra.* Indeed, in light of Section 106, the Eleventh Circuit, which otherwise would be bound by decisions of the Fifth Circuit prior to October 1, 1981 (see *Bonner* v. *City of Prichard,* 661 F.2d 1206, 1209 (11th Cir. 1981) (*en banc*)), has held that *Presbyterian Hospital* is no longer controlling. *Memorial Hospital* v. *Heckler, supra,* slip op. 3283.

[5]Section 106 of TEFRA provides:

> (a) Section 1861(v)(1) of the Social Security Act is amended by adding at the end the following new subparagraph:
>
> "(M) Such regulations shall provide that costs respecting care provided by a provider of services, pursuant to an assurance under title VI or XVI of the Public Health Service Act that the provider will make available a reasonable volume of services to persons unable to pay therefor, shall not be allowable as reasonable costs."
>
> (b) The amendment made by subsection (a) shall be effective with respect to any costs incurred under Title XVIII of the Social Security Act, except that it shall not apply to costs which have been allowed prior to the date of the enactment of this Act pursuant to the final court order affirmed by a United States Court of Appeals.

97-760, *supra,* at 431. Thus, Congress intended the new provision to ratify the Secretary's interpretation and the court decisions that previously had interpreted the Medicare statute to exclude reimbursement for Hill-Burton free care,[6] and to disapprove those decisions that had permitted such reimbursement.[7] Such clarifying legislation does not create "the inference * * * that an agency admits that it is acting upon a wrong construction by seeking ratification from Congress. Public policy requires that agencies feel free to ask legislation which will terminate or avoid adverse contentions and litigations."[8] *Wong Yang Sung* v. *McGrath,* 339 U.S. 33, 47 (1950). See also *United States* v. *New York Telephone Co.,* 434 U.S. 159, 177 n.25 (1977).

Accepting for the sake of argument petitioners' dubious premise that Section 106 constitutes an effort by Congress to apply "new law" retroactively, the new law is controlling here. Petitioners do not deny that Congress intended that Section 106 apply retroactively to pending cases; indeed, the statute and its legislative history are quite clear on this point.[9] Moreover, the federal courts repeatedly have

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[6]See, *e.g., Catholic Medical Center* v. *New Hampshire-Vermont Hospitalization Service, Inc.,* 546 F. Supp. 297 (D.N.H. 1982), aff'd, No. 82-1808 (1st Cir. May 4, 1983); *Saint Mary of Nazareth Hospital Center* v. *HHS,* 531 F. Supp. 419 (N.D. Ill. 1982), aff'd, 698 F.2d 1337 (7th Cir. 1983).

[7]See, *e.g., Presbyterian Hospital* v. *Harris,* 638 F.2d 1381 (5th Cir.), cert. denied on a different issue, 454 U.S. 940 (1981); *Metropolitan Medical Center* v. *Harris,* 524 F. Supp. 630 (D. Minn. 1981), rev'd, 693 F.2d 775 (8th Cir. 1982).

[8]In the preamble to the new regulation implementing Section 106, the Secretary indicated that he interpreted both Section 106 itself and the implementing regulation as mere clarifications of existing law. In addition, he noted that the new regulation is consistent with longstanding Medicare policy in this area, 47 Fed. Reg. 43656-43658 (1982).

[9]See page 9 note 5, *supra;* H.R. Rep. No. 97-760, 97th Cong., 2d Sess. 431 (1982).

applied changes in the law that take effect while a case is pending on appeal. See *United States* v. *The Schooner Peggy*, 5 U.S. (1 Cranch) 103 (1801). Accord, *Bradley* v. *Richmond School Board*, 416 U.S. 696, 711-716 (1974). "[I]f, subsequent to the judgment, and before the decision of the appellate court, a law intervenes and positively changes the rule which governs, the law must be obeyed * * *." *United States* v. *The Schooner Peggy, supra*, 5 U.S. (1 Cranch) at 110.[10]

Furthermore, application of Section 106 to petitioners' claims would not be unconstitutional as a breach of contractual rights to Medicare reimbursement. Assuming that petitioners had any right to Medicare reimbursement for Hill-Burton free care, that right would be statutory, not contractual. See 42 U.S.C. (& Supp. V) 1395f(b). Medicare providers do enter into an "agreement" to abide by certain rules in billing and related business practices. See 42 U.S.C. (& Supp. V) 1395cc. But this "agreement" is simply a unilateral assurance by the provider and does not obligate the

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[10]All of the courts of appeals that have considered the effect of Section 106 on pending Hill-Burton free care cost cases have applied that provision to deny providers' claims, based on application of the traditional *Schooner Peggy* principle. See *Memorial Hospital* v. *Heckler, supra*, slip op. 3283; *Saint Mary of Nazareth Hospital Center* v. *HHS, supra*, 698 F.2d at 1344; *Harper-Grace Hospitals* v. *Schweiker, supra*, 691 F.2d at 811. See also *Arlington Hospital* v. *Schweiker*, 547 F. Supp. 670, 674-675 (E.D. Va. 1982), appeal pending, Nos. 83-1439 and 83-1446 (4th Cir.); *Tarrant County Hospital District* v. *Schweiker*, No. CA 4-80-413-E (N.D. Tex. May 13, 1983), slip op. 4-6; *Beth Israel Hospital* v. *Heckler*, 560 F. Supp. 1222, 1226-1228 (D. N.J. 1983).

This Court has suggested that there may be an exception to the *Schooner Peggy* doctrine to prevent "manifest injustice." See, *e.g.*, *Gulf Offshore Co.* v. *Mobil Oil Corp.*, 453 U.S. 473, 486 n.16 (1981). But as the Sixth Circuit concluded in *Harper-Grace Hospitals* (691 F.2d at 811), that exception is inapplicable in cases like this one, in which hospitals had no reason to expect Medicare reimbursement at the time they agreed to incur Hill-Burton costs.

Secretary to provide Medicare reimbursement for any particular category of costs. The statutory entitlement to Medicare reimbursement is subject to the "reasonable cost" provision, which expressly delegates to the Secretary the authority to determine the "reasonable cost" of covered items (42 U.S.C. 1395x(v)(1)(A)). Inherent in the statutory entitlement is the possibility that the statute (or implementing regulations) might be altered in certain respects over time.[11]

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[11]The courts have recognized as much in upholding retroactive adjustments in the Medicare reimbursement system against constitutional challenges. See, *e.g.*, *Springdale Convalescent Center* v. *Mathews*, 545 F.2d 943, 955-957 (5th Cir. 1977); *Adams Nursing Home of Williamstown, Inc.* v. *Mathews*, 548 F.2d 1077, 1081 (1st Cir. 1977) ("When providers joined the new program, they knew that 'small repairs' in the regulatory scheme were likely."). See also *ibid.*, citing *FHA* v. *The Darlington, Inc.*, 358 U.S. 84 (1958) ("[T]he expectations of those who enter a regulated field are diluted by the knowledge that occasional changes will be made to better carry out regulatory purposes.").

This case does not resemble *Lynch* v. *United States*, 292 U.S. 571 (1934), cited by petitioners (Pet. 11-12). There, a true contractual obligation of the United States, *i.e.*, war risk insurance, was at issue. The Court concluded that a legislative enactment completely abrogating, through an outright repeal, all rights under the contract violated the Fifth Amendment. But it did not suggest that legislative adjustments of the sort involved here would pose a similar problem. In fact, the Court noted that mere legislative amendments to the terms of the contract posed no constitutional problem, and it observed that "[s]uch legislation ha[d] been frequent." 292 U.S. at 577. Nor do any of the other cases cited by petitioners (Pet. 12) purport to limit Congress's authority to alter or clarify the terms of heavily-regulated government benefits programs. See also *Garris* v. *Hanover Ins. Co.*, 630 F.2d 1001, 1007 (4th Cir. 1980) ("[i]t is certainly the case that a party who has 'purchased into an enterprise already regulated in the particular to which he now objects' cannot claim Contract Clause protection in that particular," quoting *Veix* v. *Sixth Ward Building & Loan Ass'n*, 310 U.S. 32, 38 (1940)). See also *FHA* v. *The Darlington, Inc.*, *supra*, 358 U.S. at 91.

There is no plausible basis for petitioners' suggestion (Pet. 13-14) that Section 106 abrogates an expectation of reimbursement upon which they reasonably relied. Hospitals did not even begin to claim Medicare reimbursement for Hill-Burton free care until the late 1970's, long after their commitment to provide such free care arose and long after enactment of the Medicare statute. Since 1977 the Secretary consistently has taken the position that free care costs are not reimbursable under the Medicare statute. No court had rejected the Secretary's view prior to the time that petitioners incurred the costs involved in this case. Petitioners' effort to portray Section 106 as a government repudiation of a simple debt, on which petitioners otherwise expected payment, simply distorts reality.[12]

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[12]See, *e.g.*, *Saint Mary of Nazareth Hospital Center* v. *HHS*, *supra*, 698 F.2d at 1344-1345 (the "alleged right" to Medicare reimbursement for Hill-Burton free care costs "simply arises out of the hospitals' reading of the Medicare Act through rose colored glasses, a reading which is to the hospitals' pecuniary advantage, and the Fifth Circuit's interpretation of the Medicare Act and the Hill-Burton Act"); *Arlington Hospital* v. *Schweiker*, *supra*, 547 F. Supp. at 675 (Section 106 did not deprive plaintiff of an enforceable property right; plaintiff had, "at best, the hope or possibility that this court might grant them the relief they sought * * *," which did not amount to a "financial obligation" that is "contractual in nature").

The courts have rejected constitutional attacks on the application of Section 106 that are similar to those made by petitioners. See *Memorial Hospital* v. *Heckler*, *supra*, slip op. 3283-3284; *Harper-Grace Hospitals* v. *Schweiker*, No. 81-1305 (6th Cir. Mar. 23, 1983), slip op. 4 (on rehearing); *Saint Mary of Nazareth Hospital Center* v. *HHS*, *supra*, 698 F.2d at 1344-1345 (neither the *Presbyterian Hospital* decision nor the hospitals' reading of the Medicare statute rises to the level of establishing a "vested right" in hospitals to receive Medicare reimbursement for Hill-Burton free care costs); *Arlington Hospital* v. *Schweiker*, *supra*, 547 F. Supp. at 674-675; *Tarrant County Hospital District* v. *Schweiker*, *supra*, slip op. 4-6; *Beth Israel Hospital* v. *Heckler*, *supra*, 560 F. Supp. at 1227-1228. Cf. *United States* v. *Darusmont*, 449 U.S. 292 (1981).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JULY 1983

DOJ-1983-07